IMF SURVEY

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Panelists Discuss Hyperinflation in Former Centrally Planned Economies

Can the release of a monetary overhang trigger hyperinflation? This question was posed by Michael Deppler, Deputy Director of the IMF's European Department I, at an IMF Vistors' Center forum held on June 25 entitled Is Hyperinflation in the Former Centrally Planned Economies Still a Threat? The other participants were Alan Gelb, Chief, Socialist Economies Reform Unit, the World Bank, and Kent Osband and Shoukang Lin of the IMF's Research Department. The panel was moderated by Shailendra J. Anjaria, Director of the IMF's External Relations Department.

The question about a monetary overhang triggering hyperinflation was originally posed in a paper by Lin and Osband, who concluded that such a development was not very likely. Deppler concurred with this view on a technical level. The monetary overhang stems from "an imbalance between the price level and the stock of money," he stated. "And hyperinflation, in order to be sustained, has to involve some flow conditions where credit is increas- *(Please turn to page 249)*

Deppler: the danger of budget deficits.

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IMF Extends ESAF Lending Period

The IMF has decided to extend the life of its concessional lending window–the enhanced structural adjustment facility (ESAF) by one year. As a result, low-income countries now have until November 30, 1993 to agree with the IMF on, and to adopt, three-year structural adjustment programs under the ESAF. At present, 72 countries are eligible to borrow under the ESAF. *(See story on page 251)*

SELECTED TOPICS

Conference Explores Issues, Obstacles, And Support for NAFTA Agreement

With negotiations for a North American Free Trade Agreement (NAFTA) entering their final stage, the Institute for International Economics and the Fraser Institute called a timely conference that

Hufbauer: a NAFTA posits a "win-win" scenario for both Mexico and the United States.

intended, according to C. Fred Bergsten, Director of the Institute for International Economics (IIE), "to take stock of where the negotiations are headed, to try to make some inputs into the final round, and to pave the way for the ratification debate." The day-long seminar, held on June 22 in Washington, D.C., featured panels of Canadian, Mexican, and U.S. experts and others, who assessed the economic, political, labor, and environmental aspects of the negotiations and speculated on the prospects and possible pitfalls the agreement might face in these three countries.

Overview of the NAFTA

Drawing on their recently published study, *North American Free Trade: Issues and Recommendations*, Gary Clyde Hufbauer, a Visiting Fellow at IIE and Marcus Wallenberg Professor of International Financial Diplomacy at Georgetown University, and Jeffrey J. Schott, a Research Fellow at IIE, offered a broad examination of the NAFTA negotiations. Hufbauer, like many of the discussants, saw the NAFTA as a natural extension of Mexico's reform efforts. The NAFTA should be viewed, he said, "as an insurance policy and a capstone for all that has gone before and is going on simultaneously."

Citing the $9 billion trade surplus that the United States is projected to run with Mexico by 1995, Hufbauer posited a "win-win" scenario for both countries, estimating a net job gain in the United States of 130,000 jobs and a net gain in Mexico of 600,000 jobs. The NAFTA would also help Mexico close its income gap with the United States and Canada. If Mexico is able to raise its income by 2 percent a year, it will close that gap by 2030.

In the United States, however, the net job gain represents the creation of 240,000 new jobs but the loss of 110,000 existing jobs. Clearly, there would be dislocations, and Hufbauer chided the U.S. administration for not providing a few "helpful leaks" about adjustment assistance. (He suggested a $900 million fund earmarked for adjustment and available over five years.) Mexico, Hufbauer added, faces a "very sharp drop" in agricultural employment within the next decade—a decrease to 15 percent from 26 percent of the total work force. Such a transition is normally accompanied by an increase in land values, he said, so that the tax system "should be able to capture those land values and convert them into urban infrastructure."

Hufbauer hoped that the NAFTA negotiations would yield an improved version of the Canada-U.S. Free Trade Agreement (one that incorporated, for example, all its dispute settlement mechanisms). The NAFTA should, he argued, provide for the rapid removal of tariff barriers and include a safeguard mechanism that provides for a "super rapid liberalization" by the country enjoying the plus side of the swing if a huge and persistent swing occurs on a broad sectoral basis in favor of one partner.

Hufbauer felt that the U.S. administration was "well behind the curve" in failing to recognize that environmental issues posed the "greatest potential deal breaker." Environment, like labor, is essentially "a money question, and the United States has to get out its wallet," Hufbauer said. In addition to accepting current environmental standards, Hufbauer recommended that the United States put up "at least an extra $1 billion a year for environmental cleanup in the obvious border areas." He also suggested a two-stage agenda to deal with environmental dumping—the concern that polluting Mexican plants might cause plants in the

United States, which are cleaner but more expensive to operate, to close down. The agenda would first require strict enforcement of existing standards and, by 1995, allow each country to put on notice those standards that it wanted the other to strengthen. This would trigger negotiations. If negotiations failed, a "green fee" (paid to the country that needed to elevate its standards) could be imposed.

Hufbauer cautioned that reports from the negotiations suggested there might be several troubling shortfalls in the potential agreement, principally in agriculture and financial services. Although agriculture offers potentially large gains, the reports suggested that "either agriculture is to be left off the table or the liberalization is to be so backloaded as to be politically not credible." He also expressed concern that the laudable privatization of Mexico's banking system may have contained "some understanding" that would shield the Mexican financial system from liberalization for a long time. This, he argued, would be intolerable for midsize companies and consumers, who would be prey to a price gouging system.

Jeffrey Schott, extending Hufbauer's analysis, called special attention to the "rules of origin" negotiations, particularly for textiles, automobiles, and computers, which he felt were headed in a dangerous and discriminatory direction. The legitimate solution to the question of how to prevent the transhipment of goods from low- to high-tariff countries was, he said, to harmonize tariffs. Focusing on rules of origin, he said, could distort trade and investment in the area and, perhaps more ominously, sponsor an emulation effect in other regions, particularly Europe.

Schott also expressed concern over the lack of attention being paid to the accession process. An accession clause would, he believed, offer the "opportunity to build a common regime and avoid a patchwork quilt of inconsistent and discriminatory trade arrangements." It would also provide a clear standard for admission to the NAFTA club.

Mexican Perspective

Rogelio Ramírez de la O, president of Ecanal, a private research company in Mexico City, and Luis Rubio, with the Centro de Investigación para el Desarrollo, an independent research institute in Mexico City, noted that Mexico is so deeply committed to an extensive program of economic reforms that in a sense it has already begun to capture some of the benefits of the free trade arrrangement. Ramírez noted that trade liberalization has had its own price effect, and economic reform, which has led to import growth, has already raised expectations, growth, and capital inflows.

But Ramírez was troubled by the specter of U.S. protectionism as well as by preliminary evidence indicating that Mexico's manufacturing and labor-intensive industries have yet to respond to the stimulus of the economic reforms. Manufacturing industries in Mexico have recorded only 0.1 percent growth since 1987, and labor-intensive industries have recorded net losses in output and employment, he said.

Rubio framed his discussion of the political dimensions of the NAFTA within two broad questions: Why reforms? Why a NAFTA? The old stability in Mexico, he noted, was rooted in the cooperation of key political groups that Rubio identified as the winners of the revolution. An "extremely well developed system of patronage" provided the glue that held the system together, Rubio said, and the system worked as long as it delivered. But by the mid-1980s, it was clear, he said, that Mexico would have to change or face social and political upheaval.

A broad new coalition—which, according to Rubio, is huge and includes, among others, the middle classes, most of labor, and some in the peasant coalition—emerged as the reform process proceeded. Rubio credited current Mexican President Carlos Salinas de Gortari with transforming this new coalition into something much more coherent. The reforms have now acquired a dynamic of their own. "The best guarantee of reform," Rubio observed, "lies precisely in the expectation that the process of reform is genuine," and those expectations can be met only if the reform process is strengthened. "There is no way to go back," he added. "Everything has changed."

Ramírez de la O: Mexico's manufacturing and labor-intensive industries have yet to respond to economic reform.

Why a NAFTA? Rubio argued that, from a purely economic perspective, a NAFTA would establish the rules of the game for Mexico and "avoid having antidumping rules invoked every time a Mexican exporter was successful." From a political perspective, however, perhaps the NAFTA's more important function

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would be as an external guarantee for the reforms. The Salinas Government, Rubio noted, realized that at the heart of the reform process was the issue of confidence, and there could be no confidence without a sense of permanence about the reforms. A clearly defined relationship with the United States would solidify and formalize this confidence.

A recent poll, Rubio said, estimated that 84 percent of the Mexican population supported the NAFTA. Rubio believed NAFTA's popularity has at least as much to do with a continued commitment to these reforms as with the specifics of the agreement.

Waverman: Canada's limited trade with Mexico has dampened its support for a NAFTA.

Canadian Perspective

Gilbert Winham, Professor of Economics at Dalhousie University, confessed that he could "just weep" when he heard of 84 percent support for the NAFTA. It is the opposite in Canada.

There is scant natural enthusiasm for the NAFTA in Canada, observed Leonard Waverman, Professor of Economics and Director of the Center for International Studies at the University of Toronto, because Canada's trade with Mexico has traditionally been very limited. While 80 percent of Canada's exports, and 70 percent of Mexico's, go to the United States, Canada's trade with Mexico has amounted to less than $3 billion annually—a fraction of its yearly $200 billion trade with the United States. Until this year Canadian-Mexican trade had, in fact, been declining.

Canada remained unconvinced of the potential for increased trade with Mexico and approached a NAFTA somewhat anxiously, Waverman noted, because "increased competition with Mexico in the U.S. market plus the upset of increased Mexican sales in the Canadian market" might pose risks for Canada. In truth, Waverman added, the United States and Mexico were free to sign a bilateral agreement, and the real question was whether Canada would remain outside the NAFTA to protect its market from Mexican exports. He maintained that Canada should take an intelligent but defensive approach—agreeing to participate in a NAFTA with an eye on the larger Latin American market.

Most at risk from the heightened competitiveness a NAFTA might generate, Waverman felt, was Canada's auto market. But he also speculated that Canada's energy sector, which has received little mention in Canada's discussion of the NAFTA negotiations, might also face increased competition. In other areas, however, such as forestry and food, Waverman indicated that there were few areas of direct competition.

Winham noted that any discussion of a NAFTA in Canada of necessity resurrected the issue of Canada's Free Trade Agreement with the United States. That agreement, the product of a Canadian initiative, is now opposed by 70 percent of the population, according to a recent poll. Waverman believed that the NAFTA could be promoted to the Canadian public as an opportunity for Canada to rewrite the Canada-U.S. Free Trade Agreement to its advantage. He thought it impossible in Canada to sell NAFTA on its own merits.

Winham cited a poll that suggested most Canadians would support an agreement that served as a stepping stone to a larger hemispheric trade arrangement. He felt Canadians could be convinced to see the longer-term benefits of participating in a multiparty agreement that would eventually lead to a broad regional arrangement.

But Winham and Waverman agreed that selling the NAFTA in Canada would not be easy, and the timing, Winham added, is "going really quite badly for Canada." The country is unlikely to implement the NAFTA until the United States does, and that is not likely to take place until early 1993. If the NAFTA and the Canada-U.S. Free Trade Agreement remain unpopular in Canada, the Mulroney Government, he speculated, may choose not to implement the NAFTA until after the next Canadian elections.

U.S. Perspective

In terms of popular support for the NAFTA, the United States is somewhere in between Mexico and Canada, noted I. M. Destler, a Visiting Fellow at the Institute for International Economics and Professor at the University of Maryland's School of Public Affairs. The 1991 vote on the extension of fast-track legislation was the latest indication, he said, "that when the chips are down [the U.S.] Congress will continue to support generally liberal trade initiatives. Executive officials, particularly the U.S. trade representative, retain substantial leeway and leadership capability within the United States if they are politically

adroit and if they remain sensitive to international and major industry concerns."

The length of the negotiations, however, has all but scuttled the original timetable for the NAFTA, which will require implementing legislation in the United States. Barring extraordinary action, Destler said, this implementing legislation now will not be introduced until the next legislative session in early 1993. The election in the intervening months may inject additional uncertainties into the process. It will certainly bring a sizable number of new members to Congress, "increasing," Destler observed, "at least at the margin, the uncertainty about how Congress will respond."

Environmental Concerns

While participants cautioned that the labor dislocations occasioned by a NAFTA would be both real, and in certain regions and sectors, significant, most discussants believed the environment would be the most contentious issue. Peter Emerson, a Senior Economist with the Environmental Defense Fund, noted that environmentalists tended to be both wary of the secrecy that surrounded these negotiations and fearful of an agreement that might reduce a national government's right to legislate in the environmental area. More specifically, they were concerned about the creation of a pollution haven in the border free trade area, and they doubted that Mexico had the technological resources to implement the necessary environmental standards.

Both Lawrence Summers, Vice President, Development Economics, and Chief Economist of the World Bank, and Dwight Lee, Professor of Economics at the University of Georgia, argued that the environmentalists were right to raise the issue but wrong to assume that free trade and a better environment were antagonistic rather than allied goals.

"It is with some trepidation that I return to the topic of the environment," Summers noted wryly. Raising environmental concerns in the context of a free trade agreement is both appropriate and likely to be constructive, he said, but "there is little doubt that the environment in the United States and Mexico will be better with a NAFTA than without one."

Environmentalists fear that increased growth will bring increased air and water pollution, but overwhelming evidence contradicts this link between growth and pollution, Summers said. "Economic growth past a minimum standard of living well below that of Mexico today is associated with improvements rather than reductions in environmental performance. The [World Bank's] *World Development Report* found a clear level of improvement after $1,000 in per capita income. Growth creates both the way and the will to improve the environment. A more prosperous Mexico will be more able and more willing to enforce its environmental regulations." More economic openness, he added, is also associated with production closer to state of the art technology, which tends to be cleaner.

A more legitimate concern, Summers felt, was effective regulation. "As we move to one world, as trade barriers come down, the pressure for some common regulatory environment becomes much stronger." He urged that common minimum standards be adopted and noted existing Mexican standards are close to U.S. standards.

The issue, Summers argued, is enforcing existing laws. "What better way to bind the enforcement of those laws," he asked, "than to have them treated as an international obligation with a clear commitment to a major party that is in a position to impose sanctions? A free trade agreement between the United States and Mexico combined with a Mexican commitment to enforce current environmental obligations would very strongly be in both countries' interests."

Lee underscored Summers' arguments by noting that free trade increases the efficiency with which resources are employed. "Does anyone seriously doubt that more competition in recent decades would have been good for the environment in Eastern Europe?" Wealthier is healthier, Lee concluded. "As countries become wealthier, they demand, and can afford, a healthier environment."

Summers: the environment in the United States and Mexico will be better with a NAFTA than without one.

Sheila Meehan,
Assistant Editor, *IMF Survey*

Copies of *North American Free Trade: Issues and Recommendations* can be obtained for $35 (cloth) and $25 (paper) from the Publications Department, Institute for International Economics, 11 Dupont Circle NW, Washington, DC 20036-1207, U.S.A.

Trend Toward Greater Convertibility Continued In 1989–90, Says IMF Study

In 1989–90, the trend toward liberalization in international payments and transfers continued, especially for nontrade current and capital account transactions. Also, the exchange rate arrangements of IMF members—developing countries in particular—tended to move further toward greater flexibility and away from single currency pegs.

These are the main conclusions of a recently published study entitled *Developments in International Exchange and Payments Systems*. Prepared by a team from the Policy Development and Review Department under the direction of Hans Flickenschild and Martin Gilman, the study presents an analysis and summary of the last two editions of the IMF's *Annual Report on Exchange Arrangements and Exchange Restrictions*, which cover developments in members' exchange and payments systems during 1989, 1990, and early 1991. It also provides a useful overview of the operations of the clearing arrangements in Eastern Europe just before the dismantling of the Council for Mutual Economic Assistance.

SDR Rates

Week Beginning	Rate of SDR Interest and Charges (percent)
July 27	6.34

The rate of SDR interest and charges is calculated weekly, by reference to a combined market interest rate, which is the weighted average of interest rates on specified short term domestic obligations in the money markets of the five countries whose currencies constitute the SDR valuation basket (U.S. dollar, deutsche mark, Japanese yen, French franc, and pound sterling). The interest rates used are those that prevail each Friday. For the latest weekly rates call (202) 623-7171.

Data: IMF Treasurer's Department

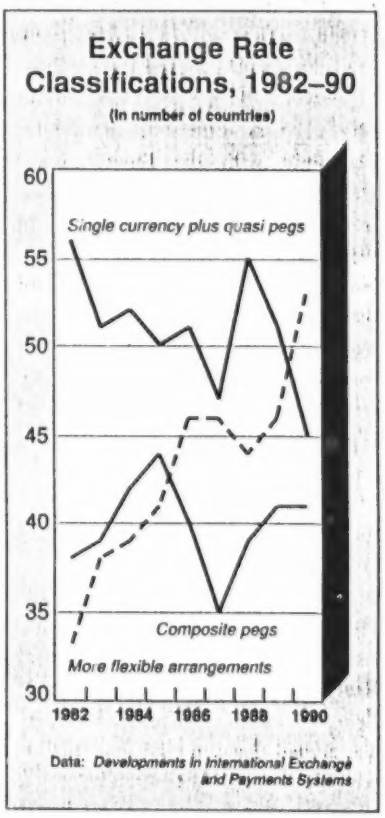
Developments in Exchange Systems

The arrangements adopted by members for determining the domestic currency price of foreign exchange can be placed into one or another of the major categories of the IMF's classification system (see box). The authors note that almost two thirds of the 28 members that changed their exchange arrangements in 1989 and 1990 adopted more flexible arrangements. The remaining 9 countries shifted primarily from managed or independent floats to pegging arrangements. In terms of the numerical importance of these groups in the IMF's membership, the countries with single currency pegs declined to 26 percent at the end of 1990, from 33 percent at the end of 1988, while countries with independent floating arrangements rose to 16 percent, from 11 percent.

The tendency to adopt more flexible exchange rate arrangements has become particularly marked among the developing countries, the authors point out. They cite two main reasons for this:

- The sharp acceleration of inflation rates during the 1980s, particularly in Africa, Eastern Europe, and the Western Hemisphere, forced many countries to depreciate their currencies (often by systematically linking their nominal exchange rates to domestic inflation) to prevent an erosion of competitiveness.
- The uncertainties associated with fluctuations in the bilateral exchange rates of the major currencies encouraged many countries to peg to a basket of currencies (rather than to a single currency) so as to mitigate the effects of those fluctuations on their economies.

In a number of developing countries, the move toward more flexible exchange arrangements was part of a comprehensive reform of their exchange systems during 1989–90 rather than the result of isolated measures. The reform typically involved the introduction of a secondary exchange market, in which the exchange rate would be determined by market forces. Occasionally, it was the result of the unification of multiple exchange rates at a substantially depreciated, market-determined rate.



In contrast with developing countries, industrial countries have tended to move toward pegged exchange arrangements since 1987–88, the authors note. They attribute this to the conviction that such arrangements foster greater discipline in domestic monetary and fiscal policies and thereby contribute to price stability. (Countries without strong anti-inflationary credibility can peg to the currency of a country with an established reputation for price stability as a means of disciplining both government policy and private sector behavior.) The authors suggest that the greater fixity of exchange rate arrangements also stems from the trend toward closer economic integration among the industrial countries, as evidenced by the European Community.

Multiple Exchange Rates

The incidence of multiple exchange rates among IMF members generally declined during the 1980s, according to the authors. They add, however, that the multiple exchange rate systems recently put in place tend to affect a larger volume of transactions than did previous practices, which were largely confined to a few types of transactions. Moreover, many of the countries that have instituted multiple exchange rate systems intend them to be transitory. These systems represent a step toward greater exchange rate realism in that they approximate market-determined solutions. Where supported by appropriate monetary and fiscal policies, they led to the marginalization, or even elimination, of the parallel exchange market in some countries.

Developments in Payment Restrictions

The trend toward the liberalization of nontrade current and capital account transactions continued in 1989 and 1990, the authors point out, "primarily because it is seen as ineffective, even counterproductive, to try to control such financial flows."

The authors draw attention, in particular, to two recent developments: the "remarkable transformation" in the former centrally planned economies, especially in Eastern Europe, where restrictions on current payments have been significantly lifted, bilateral payments arrangements broadly dismantled, and a large degree of currency convertibility established; and the liberalization of capital movements in a number of developing and industrial countries.

Considering the changes in Eastern Europe in some detail, the authors cite several instances of the following types of reforms with respect to current transactions:

- the unification of previously separate exchange rates;
- the dismantling of state monopolies on foreign trade transactions and on

Exchange Rate Classifications

Following are the different types of possible exchange rate regimes and how they work:

Single Currency Peg. The country pegs to a major currency—usually the U.S. dollar or the French franc—with infrequent adjustment of the parity. (About one third of all developing countries have single currency pegs.)

Composite Currency Peg. The country pegs to a basket of currencies of major trading partners to make the pegged currency more stable than if a single currency peg were used. The weights assigned to the currencies in the basket may reflect the geographical distribution of trade, services, or capital flows. They may also be standardized, as in the SDR and the European Currency Unit.

Limited Flexibility vis-à-vis a Single Currency. The value of the currency is maintained within certain margins of the peg. (This system applies to four Middle Eastern countries.)

Limited Flexibility Through Cooperative Arrangements. This applies to countries in the exchange rate mechanism of the European Monetary System (EMS) and is a cross between a peg of individual EMS currencies to each other and a float of all these currencies jointly vis-à-vis non-EMS currencies.

Greater Flexibility Through Adjustment to an Indicator. The currency is adjusted more or less automatically to changes in selected indicators. A common indicator is the real effective exchange rate, which reflects inflation-adjusted changes in the currency vis-à-vis major trading partners.

Greater Flexibility Through a Managed Float. The central bank sets the rate but varies it frequently. Indicators for adjusting the rate include, for example, the balance of payments position, reserves, and parallel market developments. Adjustments are not automatic.

Full Flexibility Through an Independent Float. Rates are determined by market forces. Some industrial countries have floats—except for the EMS countries—but the number of developing countries in this category has been increasing in recent years.

the provision of foreign exchange;

• the lifting of restrictions on access to foreign exchange, including for nontrade transactions.

The elimination of these and other restrictive arrangements with their inherent discriminatory features "represents an important step toward the universality of multilateral payments regimes," the authors suggest.

With respect to other countries, the authors describe a number of liberalization measures that affect import payments, exports and export proceeds, and current invisible transactions.

Turning to capital transactions, the authors note that the trend toward a more liberal environment "seems to be increasingly the result of policymakers' growing recognition of the substantial economic benefits that derive from a more open and integrated world economy...." But they also point to other factors that have helped foster liberalization—for example,

• the liberalization of financial services, which has necessitated freer capital account transactions, and technological advances, which have made it difficult to enforce restrictions on such transactions;

• the growing conviction among policymakers—especially in developing countries pursuing comprehensive adjustment programs—that an open capital account can be maintained as long as appropriate domestic policies are pursued;

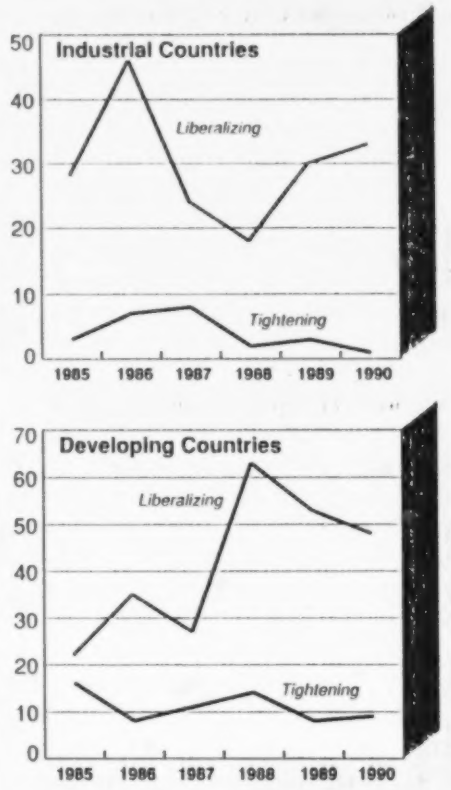
• the need to attract foreign capital, which has led to the easing of restrictions–in particular, on non-debt-creating capital inflows.

While noting that the industrial countries made "further significant progress" in freeing up capital transactions, the authors emphasize that the overall trend among developing countries in 1989–90 was, as in past years, "overwhelmingly in the direction of liberalization." The momentum toward liberalization was especially marked in Latin American countries.

Most reforms of capital controls in developing countries during 1989-90 were related to inward foreign direct investment, which has increasingly been recognized as an important vehicle for economic development. The liberalization of such investment was embraced by a broad spectrum of countries, ranging from low-income African countries to the fast-growing, dynamic economies of Southeast Asia.

Capital Controls in Industrial and Developing Countries, 1985-90

(Number of measures)



Note: These measures do not purport to indicate the economic significance of the measures taken over the period; however, they can provide an overall sense of whether member countries are taking more or less restrictive measures.

Data: *Developments in International Exchange and Payments Systems*

Bilateral Payments Arrangements

Bilateralism in payments arrangements has declined in importance in recent years, according to the authors, as more currencies have become convertible—at least for current transactions—and as financial markets have become more integrated. The authors suggest that the recent economic changes in Eastern European countries are likely to bring about further liberalizations of payment regulations. As the reforms in these countries are at an early stage, the nature of their trading relations with each other and with other countries is still evolving. But the initial steps taken—in particular, the progress toward trade at world market prices in convertible currency since 1991—"indicate the potential for a far-reaching change from bilateralism to multilateralism."

Developments in International Exchange and Payments Systems was prepared in the IMF's Policy Development and Review Department under the direction of Hans Flickenschild and Martin Gilman. Its authors are Hassan Al-Atrash, Anne-Marie Gulde, Atsushi Miyauchi, Lynge Nielsen, Mark Precious, and Eugene Spiro.

Copies may be obtained for US$20.00 (US$12.00 for full-time university faculty and students) from Publication Services, Box S-351, International Monetary Fund, 700 19th Street N.W., Washington, D.C. 20431, U.S.A.

Assessing the Risk of Hyperinflation

(continued from front page) ing at an accelerating rate. He also agreed that it was unlikely that the monetary overhang along with the process of liberalizing prices would lead to hyperinflation.

The more interesting question, he continued, is whether there is a risk of hyperinflation in the formerly centrally planned economies or, at least, of inflation getting stuck at an uncomfortably high level. This would result not only from the combination of monetary overhang and price liberalization shock but also from other features of these economies. In this context, Deppler pointed to some empirical evidence for Eastern Europe, specifically Bulgaria, Czechoslovakia, Hungary, Poland, and Romania.

It is generally accepted that Czechoslovakia and Hungary had the lowest—if any—monetary overhang when they implemented price liberalization, while Bulgaria and Romania had the largest. Poland also had low or nonexistent inflation but experienced hyperinflation before undertaking price liberalization.

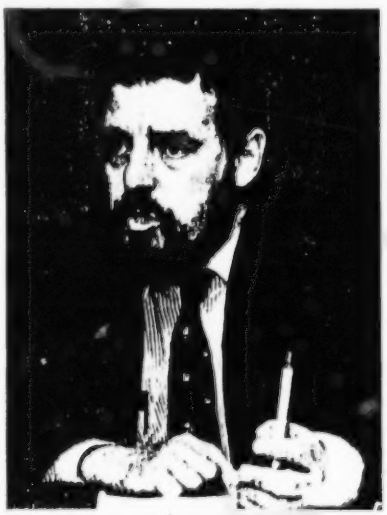
Thus, said Deppler, if one compares the inflation rates of the two pairs of countries, the former had inflation records that were far superior to the latter a year after the price liberalization. Inflation in Czechoslovakia had dropped to about 1 percent a month and in Hungary to about 2–3 percent, whereas in Bulgaria and Romania, inflation rates ranged from 5 percent to 10 percent a month. "Therefore, from a policy point of view, I would say that monetary overhang is something which you have to worry about in terms of its tendency to generate sustained inflation in the context of the broader circumstances faced by these countries. Those risks appear to be, in a sense, proportional to the extent of the monetary overhang at the beginning of the process," he concluded.

Deppler maintained that the critical issue was not the monetary overhang itself but the policies that these countries follow once they undertake the price liberalization process. In this regard, the importance of the wage response to the initial price shock has often been emphasized. Deppler agreed but pointed to other considerations that can create a sustained demand for credit. First, the locus of power within the state enterprises is shifting from the founding ministry to the workers in the process of moving to a market economy. That, together with their underlying competitive weakness, leads to a huge loss in these enterprises' profitability, to the benefit of workers in the first instance, according to Deppler. This, in turn, generates a demand for credit to finance future wages. "So there is a built-in demand for credit from state enterprises," he pointed out.

Perhaps an even greater danger comes from budget deficits, contended Deppler, pointing to the case of Poland. Between 1990 and 1992, the Polish state budget lost 10 percentage points of GNP worth of revenues, in large part because of the fall in profitability of enterprises, while social expenditures rose to 21 percentage points of GNP from about 12 percent. The resulting shock to the budget—on the order of 20 percentage points of GNP—if unchecked, will cause Poland to rely on bank financing, and will result in hyperinflation. These countries, he continued, do not have capital markets that would permit them to finance deficits of this magnitude other than through money creation.

Deppler observed that it is essential to take account of the fundamental structural weaknesses of these economies during the transition process in deciding whether there is a significant risk of hyperinflation, or of continuing high inflation. "It is clear that financial policies must be quite vigilant in curbing those tendencies," he concluded.

In Gelb's view, the release of a monetary overhang signals a fundamental change in the way the system operates. He agreed with Lin and Osband that the initial monetary overhang is a stock problem and that inflation is a flow problem. "There are three choices in dealing with the overhang," according to Gelb. "You can confiscate it, you can inflate it away, or, if you had thought about it at the beginning, you might have arranged something like swapping part of frozen financial assets for real assets which are privatized by the government."



Gelb: the inability to manage fiscal and monetary policy poses a serious risk.

Although some reform programs have proposed one or more of these

approaches, he continued, they have not actually implemented any of them. The political dynamics of reform tend to work against that sort of approach."

As for the former Soviet Union, Gelb also agreed that the overhang was not a major problem in the continuance of inflation and that the flow problem was far more serious.

In the all-important area of monetary stability, Gelb cited four potential threats. First is the tax base; the administrative capacity of the country to tax on a broad enough scale becomes more difficult as the structure of the economy changes and as the reliance on state enterprise profits is suddenly reduced. A second problem is unemployment. In many instances in which companies have been privatized, there have been dramatic declines in the work force.

Third is the problem of bad debt. Gelb believes that a serious fiscal threat is building up as credit is tightened after an initial period of very low interest rates. This is explicitly or implicitly a liability of the government that has to be met. Fourth is the problem of shrinkage of the tax base for the inflation tax. In the former Soviet Union, falls in the ratio of money to output will imply that imbalances are harder to finance through money creation without inflation.

Gelb then discussed the impact of economic disintegration on inflation. One problem is the new states' inability to manage fiscal and monetary policy. The removal of subsidies to some states as a consequence of the transition to a market economy is also exacerbating inflation. Gelb drew an analogy between the economic disintegration of the former Soviet Union and the collapse of the Austro-Hungarian empire after World War I.

Currency Units per SDR

Currency	JULY 10	13	14	15	16	17	20	21	22	23
Deutsche mark	2.16738	2.14877	2.14799	2.1467	2.14605	2.1392	2.12454	2.15842	2.147	2.14513
French franc	7.30726			7.24343	7.26503	7.22177	7.10786	7.25345	7.23016	7.24438
Japanese yen	180.507	181.126	181.014	181.23	180.894	182.106	181.311	180	180.832	182.28
Pound sterling	0.753054	0.752035	0.753451	0.753541	0.7529	0.748277	0.748588	0.759081	0.756844	0.755514
U.S. dollar	1.43773	1.44669	1.44753	1.44695	1.44715	1.45278	1.45888	1.4327	1.44239	1.44152
Argentine peso	1.42407	1.43295	1.43378	1.4332	1.4334	1.43899	1.4448			
Australian dollar	1.92596	1.93719	1.93442	1.93779	1.94508	1.9645	1.95429	1.9267	1.92998	1.92949
Austrian schilling	15.2615	15.1136	15.1166	15.1206	15.1271	15.045	14.9425	15.231	15.1134	15.0956
Bahrain dinar	0.540586	0.543955	0.544271	0.544053	0.544139	0.546245	0.548458	0.540575	0.542398	0.542012
Bangladesh taka	56.0715	56.4209	56.4537	56.4311	56.4389	56.6504	56.8877	56.0703	56.2532	56.2193
Belgian franc	44.8379	44.1783	44.2799	44.3128	44.2048	44.0995	43.7087		44.2743	44.2188
Brazilian cruzeiro	5263.03	5341.98	5391.69	5436.41	5404.48	5563.65	5824.74	5502.22	5659.29	5705.03
Canadian dollar	1.71349	1.72532	1.72705	1.72578	1.72512	1.72837	1.73435	1.71431	1.71988	1.71256
Colombian peso	1095.26	1102.65	1103.84	1103.92	1104.61	1106.4		1098.53	1102.61	1102.52
Danish krone	8.34027	8.25554	8.26974	8.28089	8.25671	8.24235	8.17579	8.27109	8.2788	8.26569
Finnish markka	5.92778	5.87356	5.87997	5.89343	5.88575	5.84398	5.81278	5.88103	5.88505	5.88428
Greek drachma	265.693	263.681	263.957	263.982	264.539	263.098	261.275	264.364	263.929	263.712
Indian rupee	37.2228	37.4548	37.4766	37.4615	37.4887	37.6125	37.7847	37.2221	37.3435	37.321
Indonesian rupiah	2924.34	2942.57	2942.83	2941.65	2942.06	2963.5	2984	2922.84	2932.38	2932.05
Iranian rial	92.3	92.3	92.3	92.3	92.3	92.3	92.3	92.3	92.3	92.3
Iraqi dinar	0.446929	0.449714	0.449975	0.449795	0.449857	0.451807	0.453435	0.44892	0.449377	0.449107
Irish pound	0.81269	0.80479	0.806154	0.804934	0.803857	0.802198	0.795777	0.809826	0.804729	0.805228
Italian lira	1640.46	1626.46	1627.73	1628.1	1630.58	1634.	1618.29	1643.	1631.26	1626.9
Korean won	1130.92	1138.69	1139.79	1139.76			1147.09	1131.84	1135.02	1133.9
Kuwaiti dinar		0.417399	0.417048	0.417734	0.417792		0.420079	0.418017	0.417817	0.418003
Libyan dinar	0.396429	0.396429	0.396429	0.396429	0.396429	0.396429	0.396429	0.396429	0.396429	0.396429
Malaysian ringgit		3.61412	3.61376	3.6152	3.61527	3.6299	3.643	3.53353	3.6041	3.60323
Maltese lira	0.436297	0.433244	0.433107	0.43379	0.433829	0.4332	0.431198	0.431133	0.432436	0.433292
Nepalese rupee	61.3911	61.7737	61.8095	61.7848	61.7933	62.0337	62.2048	61.3898	61.5901	61.5529
Netherlands guilder	2.44328	2.41887	2.42186	2.41829	2.42017	2.41031	2.38826	2.4323	2.41745	2.41988
New Zealand dollar	2.64289	2.64622	2.641	2.64283	2.64513	2.65396	2.65742	2.63258	2.6297	
Norwegian krone	8.50489	8.42191	8.44127	8.44585	8.43327	8.4145	8.34426	8.44577	8.45457	8.44298
Omani rial	0.552807	0.556252	0.556575	0.556352	0.556429	0.558594	0.560895	0.552796	0.554909	0.554264
Pakistan rupee	36.2206	36.4463	36.4675	36.4529	36.4579	36.5097	36.7479	36.2198	36.339	36.3181
Portuguese escudo	182.715	182.351	182.843	182.805	183.112	181.695	181.539	184.128	183.27	182.871
Qatar riyal	5.23334	5.26595	5.26901	5.2669	5.26783	5.29812	5.30952	5.23323	5.2583	5.24713
Saudi Arabian riyal	5.3843	5.41785	5.421	5.41883	5.41958	5.44068	5.46268	5.39419	5.40175	5.39649
Singapore dollar	2.32323	2.33409	2.33458	2.33306	2.33165	2.33985	2.34548	2.31958	2.3247	2.3258
South African rand	3.9687	3.96679	3.97706	3.97842	3.96882	3.97477	3.97412	3.97398	3.97879	3.98001
Spanish peseta	137.763	136.659	136.722	136.732	137.458	136.712	136.054	136.953	137.519	137.071
Sri Lanka rupee	63.332	63.7267	63.7637	63.7381	63.747	63.9658	64.2102	63.2307	63.5373	63.5278
Swedish krona	7.84857	7.77668	7.79495	7.79761	7.78958	7.78058	7.76758	7.80098	7.81271	7.79718
Swiss franc	1.96468	1.94797	1.94188	1.94253	1.93918	1.91894	1.87438	1.92252	1.90468	1.89982
Thai baht	36.3889	36.5434	36.5357	...	36.555	36.6827	36.7728	36.3307	36.4492	36.4705
Trinidad and Tobago dollar	6.12563	6.1638	6.16738	6.16491	6.16578	6.18975	6.2148	6.1255	6.14548	6.14178
U.A.E. dirham	5.27791	5.3108	5.31388	5.31175	5.31249	5.33318	5.35474	5.2778	5.29501	5.29182
Venezuelan bolivar	96.3998	97.0006	97.1293	97.235	97.1761	97.4815	97.9109	96.5418	96.8421	96.726

Notes: 1. The value of U.S. dollar in terms of the SDR is the reciprocal of the sum of the dollar values, based on market exchange rates, of specified quantities of the first five currencies shown. The exchange rates used for this purpose are noon rates in the London foreign exchange market. When the London market is closed, noon rates in the New York market are used. Frankfurt fixing rates are used when the New York market is closed. 2. The value in terms of the SDR of each of the other currencies shown above is derived from that currency's representative exchange rate against the U.S. dollar as reported by the issuing central bank and the SDR value of the U.S. dollar, except for the Iranian rial and the Libyan dinar, the values of which are officially expressed directly in terms of the domestic currency units per SDR.

Data: IMF Treasurer's Department

In both cases, successor states to these empires created obstacles to trade; industrial bases contracted, as did personal incomes, and governments resorted to the printing presses to solve their financial problems; unemployment rose sharply, and exchange rates came under considerable pressure.

Lin pointed out that whether or not a country's monetary, fiscal, or labor market policies are destabilizing has little to do with the monetary overhang. Whether price decontrol will lead to hyperinflation, he continued, does not depend on the initial money stock. Rather, it depends on the flow variables, such as nominal interest rates, government transfer payments, and consumption. "However," he added, "given a degree of monetary overhang, price decontrol can lead to a significant price surge initially and, therefore, a significant drop in real wages."

Osband agreed with Gelb's assessment that the inflationary threat in the former Soviet Union stems from a flow, rather than an overhang, problem. He noted, however, that many leading economists—Martin Feldstein and Rudiger Dornbusch, for example—have argued that it is an overhang problem. He pointed out that the major problem is that the statistical real wage (the nominal wage divided by the official price level) in the Soviet Union rose about 50 percent during Gorbachev's term in office without a corresponding increase in productivity. "That has to be corrected," concluded Osband, "and you can't correct that through confiscation of existing monetary balances."

Gerald R. Rosen,
Editor, *IMF Survey*

Photo credits: Denio Zara and Padraic Hughes for IMF, pages 241–245, 249, and 257.

IMF ACTIVITIES

IMF Extends ESAF Lending Period by One Year

The IMF has decided to extend the commitment period under the enhanced structural adjustment facility (ESAF)—its concessional lending window—by one year. This will allow low-income members to adopt three-year structural adjustment programs under the ESAF through November 30, 1993 rather than November 30, 1992.

The ESAF was set up in 1987 to increase substantially the amount of concessional financing available to low-income members of the IMF that undertake strong macroeconomic programs to generate economic growth and improve their balance of payments positions. The ESAF is financed through contributions from donors and lenders to a trust administered by the IMF, and it has a lending target of SDR 6 billion (about $8.75 billion). To enable all ESAF loans to be available at concessional interest rates, subsidy contributions are received by the ESAF Subsidy Account.

Before the recent expansion of ESAF eligibility, 61 low-income members were eligible to qualify for loans under the ESAF. In April 1992, the IMF added 11 countries to those already eligible. These additional countries, some of which are new members, share similar characteristics—such as low per capita incomes, high debt burdens, and protracted balance of payments difficulties—with those members already eligible.

To date, 20 IMF members have made use of ESAF financing: Bangladesh, Bolivia, Burundi, The Gambia, Ghana, Guinea, Guyana, Honduras, Kenya, Lesotho, Madagascar, Malawi, Mauritania, Mozambique, Niger, Senegal, Sri Lanka, Tanzania, Togo, and Uganda. Total commitments under ESAF arrangements are SDR 2.6 billion (about $3.8 billion), of which SDR 1.6 billion (about $2.3 billion) has been disbursed.

IMF Members Eligible for Assistance Under the ESAF

Afghanistan	Madagascar
Albania	Malawi
Angola	Maldives
Bangladesh	Mali
Benin	Mauritania
Bhutan	Mongolia
Bolivia	Mozambique
Burkina Faso	Myanmar
Burundi	Nepal
Cambodia	Nicaragua
Cape Verde	Niger
Central African Rep.	Nigeria
Chad	Pakistan
China	Philippines
Comoros	Rwanda
Côte d'Ivoire	St. Kitts and Nevis
Djibouti	St. Lucia
Dominica	St. Vincent
Dominican Rep.	Sao Tome & Principe
Egypt	Senegal
Equatorial Guinea	Sierra Leone
Ethiopia	Solomon Islands
Gambia, The	Somalia
Ghana	Sri Lanka
Grenada	Sudan
Guinea	Tanzania
Guinea-Bissau	Togo
Guyana	Tonga
Haiti	Uganda
Honduras	Vanuatu
India	Viet Nam
Kenya	Western Samoa
Kiribati	Yemen
Lao P.D.R.	Zaire
Lesotho	Zambia
Liberia	Zimbabwe

From The Executive Board . . .

Kazakhstan: New Member. The Republic of Kazakhstan today became a member of the IMF. The IMF's Articles of Agreement were signed in Washington, D.C. on behalf of Kazakhstan by Mr. Beisenbai Izteleuov, Deputy Chairman of the High Economic Council to the President of Kazakhstan. The initial quota of Kazakhstan in the IMF is SDR 165 million (about $239 million).

With the admission of Kazakhstan, the membership of the IMF now totals 167 countries. The total of members' quotas in the IMF is SDR 96,405.05 million (about $139,469 million).

Press Release No. 92/56, July 15

Zambia: Economic Program and Accumulated Rights. The IMF has endorsed Zambia's economic and financial program and approved the accumulation of "rights" for Zambia for up to a maximum of SDR 836.9 million (about $1,211 million), the level of its arrears to the IMF as of July 1, 1990. Upon successful implementation of this program, which runs through March 1995, and prior clearance of its arrears to the IMF, as well as meeting all other requirements for using IMF resources, Zambia would be eligible to "encash" the accumulated rights under a successor IMF arrangement.

Today's decision was taken under the rights approach endorsed by the Interim Committee of the Board of Governors of the IMF and the World Bank at its May 1990 meeting. Through this procedure, a member with protracted arrears to the IMF at the end of 1989 can earn rights based on its performance under an IMF-monitored economic program. The accumulated rights would then be encashed as part of the first disbursement under a successor IMF-supported program financed from the IMF's general resources or, for eligible members such as Zambia, from a blend of general resources and concessional structural adjustment facility and enhanced structural adjustment facility resources.

Zambia may—based on program performance during 1992—accumulate rights up to the equivalent of SDR 251.1 million (about $363 million). Further rights would be phased over the remaining period of the program. Zambia has met all financial obligations falling due to the IMF this year. It eliminated its arrears to the World Bank on January 31 1992 and has since met its financial obligations falling due to the Bank. Zambia intends to continue to meet such obligations to the IMF and the World Bank as they fall due, as well as to reduce its arrears to the IMF by SDR 84 million (about $121.6 million) by the end of 1993.

The IMF previously endorsed a rights accumulation program for Zambia in April 1991. However, there were slippages in policy implementation in the run-up to the multiparty elections at the end of October 1991, and Zambia failed to accumulate any rights under that program. The Government that took office following the elections requested that the previous program be canceled and replaced with the present one.

In early 1992, Zambia and most of southern Africa were hit by a very severe drought. Despite this difficult situation, the new Government has implemented a series of key measures necessary to reestablish economic stability and set the stage for economic recovery. Subsidies will no longer place a major burden on the budget; fertilizer subsidies have been eliminated and maize meal prices increased. A fundamental reform of personal taxation has been implemented, an essential step to establishing a viable tax system, and important actions have been taken to liberalize the exchange system and encourage noncopper exports.

In view of Zambia's extremely heavy external debt-servicing burden and the expected longer-term downturn in copper production, the Government regards the diversification of sources of foreign exchange earnings as crucial to the adjustment effort. Policies that are expected to contribute to this objective and to a more effective use of foreign exchange include further liberalization of exchange and trade policies; establishment of a unified exchange system with a market-determined exchange rate; and creation of an environment conducive to domestic and foreign private investment in both mining and nontraditional export industries.

Reform of the state enterprise sector is a further major effort designed to transform the economy. Most state-owned enterprises will be privatized or liquidated over the next five years. A few, mostly public utilities, will be retained in the public sector, but restructured and strengthened. A Privatization Act has been approved by Parliament, and a new privatization agency will be responsible for undertaking all activities relating to privatization. Ten enterprises, out of the 140 that are to be divested, will be completely privatized by the end of 1992, and a further 10 are being prepared for offer for sale by the end of the year.

The implementation of Zambia's program can be expected to have a positive impact in the coming years on employment and income generation by increasing overall economic activity, labor intensity, nontraditional exports, and the role of the private sector. In the short run, however, the impact of the drought and the reduction of subsidies will affect the rural and urban poor. To address this, the Government has devised an approach that will, with the assistance of donors, temporarily provide free or reduced-cost maize to the most vulnerable groups; channel part of the savings from the abolition of subsidies into programs to aid the poorest of the poor; advise and retrain retrenched workers; and implement, with World Bank and donor assistance, a program of small-scale labor-intensive public works in water, sanitation, health, and education. Also, the Government intends to increase steadily the share of budgetary expenditures going to health and education over the medium term, particularly for the neediest groups.

Zambia joined the IMF on September 23, 1965, and its quota is SDR 270.3 million (about $391 million). Zambia's outstanding financial obligations to the IMF, including overdue obligations, currently total SDR 920.7 million, (about $1,332 million).

Press Release No. 92/57, July 17

Greece: Article VIII Status. The Government of Greece has notified the IMF that it has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the IMF's Articles of Agreement.

IMF members accepting the obligations of Article VIII undertake to refrain from imposing restrictions on the making of payments and transfers for current international transactions or engaging in discriminatory currency arrangements or multiple currency practices without IMF approval.

Among the main objectives of the IMF are to facilitate the expansion and balanced growth of international trade, and thereby contribute to high levels of employment and real income; and to assist in the establishment of a multilateral system of payments in respect of current transactions between IMF members. In seeking to achieve these objectives, the IMF encourages the elimination of restrictive exchange practices among its member countries.

Greece is the seventy-second member of the IMF to assume Article VIII status.

By accepting Article VIII status, Greece gives confidence to the international community that it will pursue sound economic policies that will obviate the need to use exchange and payments restrictions on current transactions, and thereby contribute to a multilateral payments system free of restrictions.

Press Release No. 92/58, July 22

Stand-By, Extended, Structural Adjustment Facility (SAF), and Enhanced Structural Adjustment Facility (ESAF) Arrangements as of June 30, 1992

(million SDRs)

Member	Date of Arrangement	Expiration Date	Amount Agreed	Undrawn Balance
Stand-by arrangements			**5,118.69**	**4,025.36**
Barbados	February 7, 1992	May 31, 1993	23.89	15.36
Brazil	January 29, 1992	August 31, 1993	1,500.00	1,372.50
Bulgaria	April 17, 1992	April 16, 1993	155.00	124.00
Cameroon	December 20, 1991	September 19, 1992	28.00	20.00
Costa Rica	April 8, 1991	September 30, 1992	33.64	8.00
Côte d'Ivoire	September 20, 1991	September 19, 1992	82.75	49.65
Czechoslovakia	April 3, 1992	April 2, 1993	236.00	218.00
Dominican Republic	August 28, 1991	March 27, 1993	39.24	39.24
Ecuador	December 11, 1991	December 10, 1992	75.00	56.44
Egypt	May 17, 1991	November 20, 1992	278.00	130.80
El Salvador	January 6, 1992	March 5, 1993	41.50	41.50
Gabon	September 30, 1991	March 23, 1993	28.00	24.00
India	October 31, 1991	June 30, 1993	1,656.00	1,386.00
Jamaica	June 28, 1991	September 30, 1992	43.65	10.95
Jordan	February 26,1992	August 25, 1993	44.40	29.60
Mongolia	October 4, 1991	December 31, 1992	22.50	8.75
Morocco	January 31, 1992	March 31, 1993	91.98	73.58
Nicaragua	September 18, 1991	March 17, 1993	40.86	23.83
Panama	February 24, 1992	December 23, 1993	93.68	66.63
Papua New Guinea	July 31, 1991	September 30, 1992	26.36	26.36
Philippines	February 20, 1991	December 31, 1992	264.20	150.95
Romania	May 29, 1992	March 28, 1993	314.04	157.02
Extended arrangements			**12,625.05**	**6,480.64**
Argentina	March 31, 1992	March 30, 1995	2,149.25	2,134.25
Hungary	February 20, 1991	February 19, 1994	1,114.00	556.77
Mexico	May 26, 1989	May 25, 1993	3,729.60	466.20
Poland	April 18, 1991	April 17, 1994	1,224.00	1,147.50
Tunisia	July 25, 1988	July 24, 1992	207.30	51.83
Venezuela	June 23, 1989	March 22, 1993	3,857.10	1,851.50
Zimbabwe	January 24, 1992	January 23, 1995	343.80	272.60
SAF arrangements			**76.44**	**39.95**
Burkina Faso	March 13, 1991	March 12, 1994	22.12	15.80
Comoros	June 21, 1991	June 20, 1994	3.15	2.25
Lao P.D.R.	September 18, 1989	September 17, 1992	20.51	—
Rwanda	April 24, 1991	April 23, 1994	30.66	21.90
ESAF arrangements			**1,853.56**	**609.30**
Bangladesh	August 10, 1990	August 9, 1993	345.00	57.50
Bolivia	July 27, 1988	July 2, 1992	136.05	—
Burundi	November 13, 1991	November 12, 1994	42.70	29.89
Guinea	November 6, 1991	November 5, 1994	57.90	49.22
Guyana	July 13, 1990	July 12, 1993	81.52	17.71
Kenya	May 15, 1989	August 1, 1992	261.40	45.23
Lesotho	May 22, 1991	May 21, 1994	18.12	13.59
Malawi	July 15, 1988	September 29, 1992	66.96	5.50
Mozambique	June 1, 1990	May 31, 1993	100.65	30.50
Sri Lanka	September 13, 1991	September 12, 1994	336.00	224.00
Tanzania	July 29, 1991	July 28, 1994	181.90	128.40
Togo	May 31, 1989	May 19, 1993	46.08	7.68
Uganda	April 17, 1989	November 27, 1992	179.28	—
TOTAL			19,673.74	11,155.25

Note: Figures may not add to totals because of rounding. Data: IMF Treasurer's Department

Ten Countries Drew on IMF Resources

The IMF disbursed a total of SDR 391.0 million to 10 countries in June. Of this, SDR 264.4 million was disbursed under the General Resources Account, including SDR 187.6 million under stand-by arrangements to Jamaica (SDR 10.9 million), Jordan (SDR 7.4 million), Mongolia (SDR 2.5 million), Panama (SDR 9.8 million), and Romania (SDR 157.0 million). A further SDR 76.8 million was disbursed to Romania under the compensatory and contingency financing facility.

A total of SDR 126.6 million was disbursed under the enhanced structural adjustment facility to Bolivia (SDR 22.7 million), Burundi (SDR 8.5 million), Guyana (SDR 8.9 million), Mozambique (SDR 30.5 million), and Sri Lanka (SDR 56.0 million).

Camdessus Highlights Importance of Social Policy in Address to ECOSOC

Following is a speech prepared for delivery by Mr. Michel Camdessus to the High-Level Meeting of the UN Economic and Social Council (ECOSOC) in New York on July 7, 1992:

Along with many others, who have not had the privilege of addressing this gathering, we are fortunate to be carrying out our functions at a time when the future of the world seems to be brightening somewhat in several areas:

- international tensions are easing and—so we can hope, at least—freeing up enormous resources for the work of development;
- public support is growing for better-designed economic policies. I have talked about this silent revolution on many occasions, and now we see that when such policies are implemented with perseverance, the lot of developing countries improves;
- democracy is at last gaining ground, and with this come the rejection of corruption and the demand for more transparent and less costly government.

We are aware of all this, but we are also aware that any period of transition is a time of tension between outworn systems and methods and a world that is trying to find itself. Current events serve to remind us daily how fragile are the opportunities for peace and economic progress, and how easily broken the spirit of reform. All the more reason for us to ask ourselves, given such a scenario, how our institutions can facilitate this transition and contribute further to the sustainable economic growth proposed by the Rio conference as an objective. The conference emphasized also that relief of poverty and economic well-being are not the only aspects of progress to which man aspires. There is also environmental protection, and many other values: it is to this wider view of growth that I refer when I often speak about high-quality growth.

What must we do to achieve this? In light of our experience in recent years, it seems to me that we could gain much in terms of effectiveness if we were to commit ourselves to establishing a better-ordered system of international cooperation, composed of a combination of the following four pillars, which are inseparable: well-conceived macroeconomic reforms, an effective development strategy, a system of international trade that is universally unrestricted, and a social policy—in other words, a system that could give a fully human dimension to the first three elements. My message today will be that after having exhausted ourselves over the past decade restating the first three pillars of our structure, it is high time we restated the fourth, if we want the structure to be solid.

In view of all these considerations, I can only agree, unreservedly, with the Secretary-General's statement in his preface to the report on "Enhancing International Cooperation for Development" that the complementary functions of the various agencies of the United Nations can and must be better used.

* * * * *

I mentioned four pillars. The IMF is one.

First, a word about the IMF's effort to adapt during recent years and over the last few months.

Everyone knows that our special task is to encourage the worldwide implementation of sound economic policies of adjustment and to support them by mobilizing the assistance of the international community for each of our member countries. For us, as well as for all UN organizations, the 1980s meant adaptation to our new tasks in indebted countries, in countries in transition to a market economy, and, for several months now, in the 15 states of the former Soviet Union.

As we did so, we tried to do a better job of incorporating the social dimension and concern for the environment into our programs, in cooperation with the World Bank and UN agencies; we also strengthened the instruments that we use particularly to assist the poorest, most disadvantaged countries, and we are now trying to come up with a more relevant analysis of the burden of unproductive expenditure, particularly military expenditure, to assist our member countries in reaching decisions in this regard. Further progress will be necessary!

If almost eighty countries are currently implementing or preparing economic reform programs with IMF support, it is because they are experiencing serious difficulties, but this also shows that they are trying to solve them, using serious methods, and that they believe in the success of this strategy. As we have documented, after such programs were implemented with perseverance over several years, they began to bear fruit: economic aggregates stabilized, medium-term growth prospects improved, and poverty receded. We can expect a genuine, in-depth improvement in the economy concerned as a result of these programs. But that can never be taken for granted. In many cases, much still remains to be done, and now, as soon as they feel they are ready, we are

going to have to apply ourselves to helping, to the best of our ability, those countries whose reform efforts are inadequate at the moment.

Furthermore, it is absolutely essential that the industrial countries improve their economic performance; in present circumstances, adjustment must be universal; such improvement is not just for their own sake but is also for strong world growth as a whole. I am particularly struck by the phenomenon—so new in 1992, and certainly underemphasized up to now—that it is the developing countries which are currently exerting a locomotive effect on a world economy weakened by the recession in the industrial countries. It really is time for the industrial countries to regain their locomotive role by putting their economies on a growth path.

This, Mr. Chairman, is what we in the IMF are working on. My colleague from the World Bank will surely speak about the remarkable work his institution is carrying out to promote development and combat poverty in the world, and I hardly need to stress the importance of the GATT's [General Agreement on Tariff and Trade] role in ensuring that all countries benefit from progress toward more open global trading conditions more widely subject to multilateral discipline. May I simply stress, from the IMF standpoint, how critical this time is for the Uruguay Round. The principle of multilateralism will be undermined if it fails. But should these negotiations lead to an agreement, confidence will be restored, just at the right time, and will brighten the global economic prospects. In the present economic situation, faced with today's challenges, the world cannot allow itself the luxury of a failure or, what amounts to much the same thing, postponing its success until tomorrow.

Let us imagine that it is successful. What, then, would we still be lacking in order to feel that we have—more or less—the instruments we need to support this strategy for sustainable, high-quality growth in the final years of this century? Clearly, a lot of things! Let me emphasize two of them. Two missing links, one we know well, the other less well.

The well-known missing link is obviously the insufficient amount of official development assistance (ODA) and the difficulty our multilateral institutions have in matching their capital resources to their immediate responsibilities. Whatever the decisive role of domestic saving in the development process, whatever the potential role of private investment, they will not emerge in the developing countries, nor in those countries in transition to a market economy, unless aid primes the pump and plays its role as a catalyst. Official development assistance is more essential than ever, and should be emphasized because it is now possible to increase it, since the prospects for peace free up resources. Also, so long as overindebtedness is compounding the extreme poverty of many countries, we cannot allow the illusion to spread that the fate of the poorest countries can be seriously improved if we try to deal with their problems only with resources at market rates of interest. There has to be some grant element in the solutions we propose to them.

Therefore, I believe that an increase in official development assistance is needed, more than ever, and especially by those countries that are still short of the 0.7 percent target. However, there is another way to increase the effectiveness of too-scarce ODA resources: developing countries which have made progress, thanks to ODA, could gradually learn to do without it in future and thus release resources for others. That might be a form of south-south solidarity worth looking into.

"official development assistance is more essential than ever, and . . . it is now possible to increase it."

Irrespective of any increase in ODA, it is of the utmost importance that all forms of official financial resources *be used more efficiently*. Donors, as well as recipients, can act without delay to ensure that assistance is targeted more accurately and helps to attain the economic and social objectives of the beneficiaries. We must all be guided by the golden rule that resources are limited and they must be used as wisely as possible.

Mr. Chairman, let us suppose for a moment that some impulse—not just of generosity, but of clearsightedness—causes an improvement in global performance in terms of ODA. One link would still be missing in order for our adjustment, development, and trade-opening efforts to have a genuinely more human dimension; the fourth pillar, the social pillar, still needs to be strengthened.

Here again, allow me to speak from experience. When I look at the many operations—one could say rescue operations—on behalf of countries in difficulties that I have known over the past five years, and I think of our varied experiences in places like Uganda, Mozambique, Bolivia, Peru, Viet Nam, and many others, I can say that the essential missing element—despite the admirable efforts of the United Nations and its specialized agencies—is a sufficient regard for the short-term human costs involved during adjustment or transition to a market economy. Yes, we still have to make a major effort to see to it that the social aspects of our strategies are dealt with on a coordinated basis, with suitable structures and means of financing. For the moment, we are a long way from that: the attention given to these problems has

been disjointed or sporadic, the social component of our interventions—and I mean all of us, bilateral and multilateral donors—is financially inadequate, comes too late, and sometimes is disorganized.

Of the social problems that merit special priority in the four-pillar strategy I am suggesting, I wish to mention:

1. Strengthening the links between the structural adjustment and development efforts and the problems of regional security: assistance for demobilization operations, assistance to refugees, and, more generally speaking, more efficient inclusion of humanitarian aid when macroeconomic programs are being launched in the aftermath of political upheavals or wars. The IMF and the IBRD [International Bank for Reconstruction and Development] have attempted to address these aspects in the context of adjustment programs and have enhanced collaboration with the United Nations and its specialized agencies. The UNDP [United Nations Development Program] has really brought social issues and problems of development to the fore in its *Human Development Report*, but perhaps we should be honest enough to recognize that with our multiplicity of programs, our duplicated efforts, and our petty differences, we may have contributed to discouraging contributions, or at least to providing excuses for those who were just looking for ways to avoid contributing.

2. The unevenness of international technical and financial support for the social aspects of programs and for installing what we call social safety nets, as well as the lack of solid, credible structures for stimulating assistance.

Camdessus: it is vital to give attention to the human costs of adjustment or transition.

If this precarious situation is to be faced, three elements have to be combined:

- a renewed collective awareness of the importance of the social content of adjustment programs;
- credible and institutional arrangements to manage these problems; and
- financial resources.

Mr. Chairman, do not let us be intimidated by the financial aspect of these problems and allow me, in conclusion, to venture a suggestion: if we strengthen our coordination, if we are perceived to genuinely devote ourselves to what is essential without duplicating effort, working so that our actions are mutually reinforcing, the financing will follow .... or, at least, more of it will follow.

Mr. Chairman, let us get down to work immediately with the means that we do have: the renewed ACC [Administrative Committee on Coordination] and ECOSOC are part of these means, as is the Sustainable Development Commission, in which the Rio conference placed great hope and which will certainly have a major role to play as well. The proposed "social summit" can contribute to this recognition of the need to deal with social and economic problems together; it can also bring a spirit of decisiveness to ideas for reorganizing existing institutions and their cooperation; last, it can do its part in securing a higher priority for larger allocations of resources in support of these—so far greatly neglected—social tasks. Therefore, I personally hope that this summit takes place: its contribution will be pivotal in giving our system a solid fourth pillar.

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